Embassy of Japan

Japan's Changing Agricultural Policies

The high cost of farming and increased openness to world trade have put Japan's agricultural producers under constant competitive pressure. As a result, the number of farms in Japan dropped by 14 percent from 1990 to 1998, and Japan is increasingly dependent on food imports to meet consumers' nutritional needs. Japan is the world's largest importer of agricultural products ($33 billion in 1999). The government is revising its agricultural policies and programs in an attempt to stem the decline in self-sufficiency in food production. Japan also seeks to ensure that its farm program expenditures will be exempt from reductions required under current and proposed rules of the World Trade Organization (WTO). In its February 2001 notification to the WTO, Japan contended that major programs subject to reduction have been replaced by new programs that are less trade-distorting and thus exempt from cutbacks.

New National Food Policy

In July 1999, Japan adopted the Basic Law on Food, Agriculture and Rural Policy, which "thoroughly, reviews the postwar agricultural policies…and sets up a new policy-making scheme under…four basic principles," which include securing a stable food supply, fulfillment of the multiple functions of agriculture, sustainable development of agriculture, and promotion of rural areas. These principles reflect two themes stressed by Japan's government: 1) national food security requires that domestic agriculture produce some minimal level of output, and 2) agriculture is multifunctional, not only producing food and fiber, but also serving, for example, an environmental purpose.

Major initiatives are underway to change the structure of farming and to make it more efficient. Under its current structure, Japan's agriculture has such high producer costs that without protection it could not compete with most imported products. Without barriers to trade, Japan's consumers could rely almost completely on imports to satisfy their food needs—and save money.

Japan is raising economic and political arguments that even with its current uncompetitive structure, agriculture's functions beyond producing food for the market make it worth preserving. For instance, Japan cites the value of rice paddies in controlling flooding and the need to maintain agriculture in order to preserve the economic health of rural villages.

Japan's new policy stance explicitly recognizes that food security depends on continued imports and stocks, as well as on maintaining domestic production capability. During the current WTO discussions to continue the agricultural reform process, Japan is arguing that greater dependence on imported food (currently supplying 60 percent of caloric intake) could be dangerous if extreme events, such as war, cut trade links.

The goal of the Basic Law is preserving Japan's current level of domestic food production and not allowing the rate of food self-sufficiency (the share of consumption produced domestically) to decline further. Given this objective, the Basic Law encourages greater use of market mechanisms to increase the efficiency of the farm sector. In the last 3 years, a series of commodity-specific laws has changed the way the government supports agriculture. In general, the new policies set up programs to provide income support and income insurance for production of specific commodities instead of intervening to support market prices.

The Rice Farming Income Stabilization Program, which began in 1998, is a major example of the new commodity policies. Rice farmers receive some compensation if market prices fall below a "standard" price, calculated as the average market price of the preceding 3-year period. In the event of below-average prices, producers can collect 80 percent of the difference between the current-year price and the standard price, multiplied by the farmer's current-year production. Payment comes from the Rice Farming Income Stabilization Fund, supported by contributions from participating farmers (2 percent of the standard rice price per unit of the farmer's output) and the government (6 percent of the standard rice price per unit of total domestic production) each year. Participation in the Income Stabilization Program is voluntary.

Because rice surpluses are a chronic problem, production-limiting rice diversion programs have a long history in Japan. Farmers choosing to participate in the Rice Farming Income Stabilization Program are required to participate in the Rice Supply-Demand Stabilization Program, which diverts some of their land

away from rice. Japan asserts that the program linkage between government assistance and limitations on rice production puts rice policy into the WTO "blue-box" category—i.e., the programs are exempt from domestic support limits because they involve limits on production. Some rice farmers with efficient operations have chosen not to participate in the rice programs because they do not wish to divert any land from rice production or to contribute to the rice fund.

Diversion can be to crops, fruit trees, vegetables, or fodder, or to conservation (fallow status) or other uses (e.g., landscape enhancement). Government payments per hectare (revised annually) vary according to the use made of diverted land and reflect government preferences for growing alternative commodities.

A farmer could divert a rice field to another crop, receive revenue from selling that crop plus the diversion payment, and still participate in the income stabilization program to receive payments from rice farming on other fields. Surpluses are also a problem for milk, fruits, and vegetables at times, and programs for those commodities include setting maximums for production and rewarding farmers who limit production.

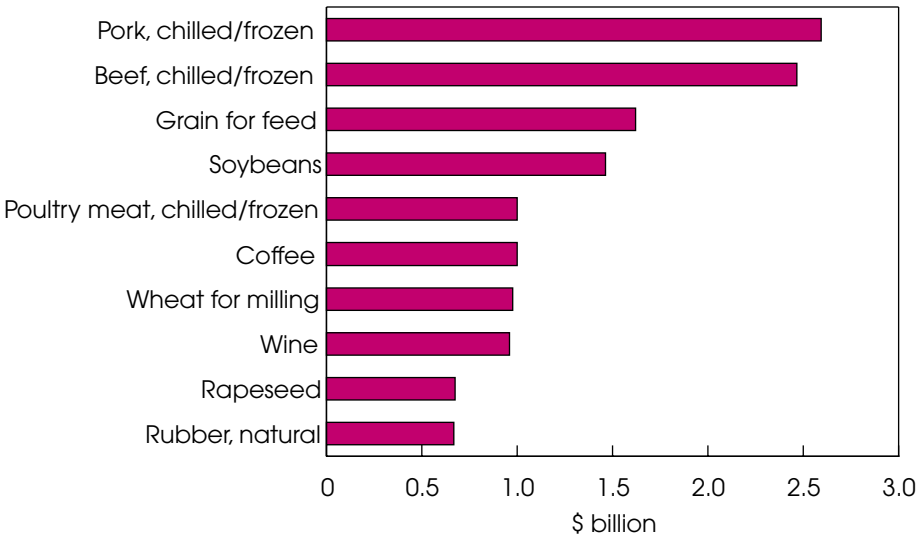
For other commodities, the concern is declining production, not overproduction. For example, the new soybean program that was introduced in 2000 works like the rice income program described above, but has no requirement to limit or divert soybean area. Instead, diversion from rice to soybeans is encouraged. Farmers participating in the Soybean Farming Stabilization Program receive compensation for 80 percent of a price drop when prices fall below the standard price. Annual payments into the Fund are 3 percent of the standard price from farmers and 9 percent of the standard price from the government. And farmers growing soybeans on a diverted rice field also get a direct payment from the diversion program for not planting rice. The same type of income program is to be introduced for wheat.

The new income stabilization programs for rice and soybeans are typical of most policies for agricultural commodities in Japan. The programs rely more on competitive market pricing than did Japan's old policies. For example, the old soybean deficiency payment was based on a fixed target price based partly on estimates of average costs of production. The program paid 100 percent of the difference between the target price and the actual market price received, so farmers had no strong incentive to raise quality or to produce for a niche market.

Under the new system, farmers participating in the income stabilization program get only 80 percent of the calculated price differential and thus bear a 20-percent share of the risk of revenue loss from a drop in prices. Because the standard price is an average of previous actual market prices rather than a support price based on costs, farmers today have a greater incentive to keep costs low and to achieve high sales prices—e.g., through their choice of product mix or through development of a marketing strategy.

For other agricultural products, administered prices set by the government were intended to guide market prices, and the government sometimes stepped in to buy up output when market prices fell below a designated level, raising prices to buyers as well as to sellers. In theory, Japan's commodity markets are supposed to see less of this intervention in the future.

Pork and Beef Are Japan's Leading Agricultural Imports



Annual average value of top 10 agricultural imports, 1997-99.

Economic Research Service, USDA

Changes in Japan's Import Policies

Japan has an extensive set of trade policies to regulate imports of agricultural commodities. When the Uruguay Round Agreement on Agriculture (URAA) was ratified, Japan agreed to replace quantitative restrictions with tariffs and tariff-rate quotas (except for rice), and to reduce the level of protection afforded by the tariffs and quotas during 1995-2000. Since the URAA went into effect, Japan has made further changes in its trade rules, including:

- a reduced role for the Food Agency, the state-trading arm of the Ministry of Agriculture, Forestry, and Fisheries;
- establishment of a tariff-rate quota for rice;
- extensive use of URAA safeguard mechanisms to raise tariffs; and
- reduction of phytosanitary barriers against some horticultural imports.

Domestic wheat production is now sold in private-sector transactions instead of being sold to the Food Agency. Imports of

World Agriculture & Trade

Policies Affecting Imports and Production of Major Agricultural Commodities in Japan

		Trade policy				
	Total imports	Tariff-rate quota[1]	Tariff or within-quota tariff	Over-quota tariff[2]	Maximum price markup	Average import price
	1,000 tons	*1,000 tons*	*Percent*	*Yen/kg*	*Yen/kg*	*Yen/kg*
Rice[3]	693	682	0	341	292	43
Wheat[3,4]	5,900	5,740	0	55	53	19
Barley[5]	1,600	1,369	0	39	34	16
Corn[5]	16,000	Customs supervision	Higher of 50% or 12 yen/kg			13
Sorghum	2,100	None	3			12
Soybeans	4,750	None	0			27
Rapeseed	2,100	None	0			25
Beef	1,000	None	38.5			388
Pork	880	None	4.3% + duty[6]			530
Poultry meat	550	None	8.5-11.9			170
Milk	0	Quota[7]	25	114 + 21.3% tariff		600
Sugar[8]	1,573	Gov't purchase	0			21
Peanuts	100	75	10	617		108

		Domestic policy				
	Total production	Producer quota	Diverted area	Income stabilization program	Paid diversion from rice	Self-sufficiency[9]
	1,000 tons	*1,000 tons*	*1,000 ha*			*Percent*
Rice	8,636		1,063	Yes		93
Wheat	600			Yes	Yes	9
Barley	160			Yes	Yes	9
Corn	1			No	No	0
Sorghum	0			No	No	0
Soybeans	190			Yes	Yes	4
Rapeseed	1			Yes	No	0
Beef	534			Yes		35
Pork	1,270			Yes		59
Poultry meat	1,160					68
All milk	8,500			Yes		100
Manufacturing		2,270				
Sugar	795			Yes	No	34
Peanuts	27				No	21

2000 data. Yen/US$ = $107.42.

1. Within the tariff-rate quota, the simultaneous buy-sell (SBS) quota is 120,000 tons for rice, 120,000 for wheat, and 600,000 for barley. 2. The government in general has waived the over-quota tariff. 3. Rice, wheat,and barley imports under quota are subject to decisions of the state trading organization. 4. Actual wheat markup is 25 yen/kg (the cif import price minus the resale price for nonfeed-use wheat). 5. In practice, corn is imported with no tariff. Customs supervision limits the amount available for the sweetener industry. 6. If the pork import unit price is below a government-set standard import price (482 yen/kg for pork cuts), duty is charged to make up the difference. 7. Fluid milk is included in a general quota for several dairy products. 8. Sugar imports must be sold to a government agency, which resells to private firms at a higher price. 9. Production divided by the sum of production and imports.

Economic Research Service, USDA

Japan's Pork-Sector Policies

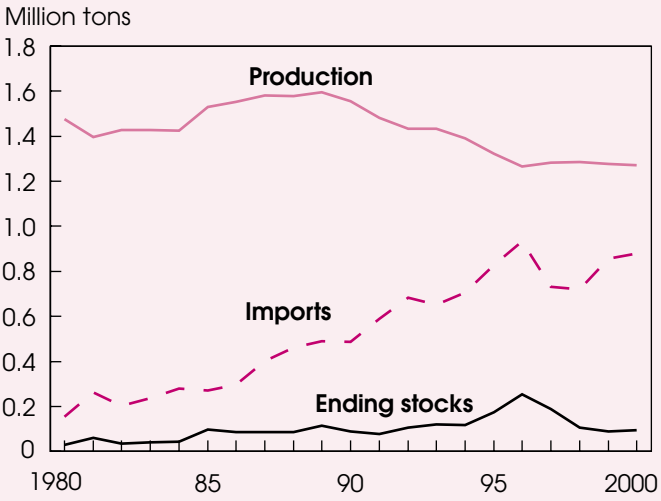
Japan's pork market illustrates the role of both import and domestic measures in protecting commodity markets, and also the very rapid restructuring of agriculture that is occurring as market prices decline. Japan's pork imports—the world's largest—grew steadily until 1997, replacing domestic production. Since then, production declines in Japan have been insignificant and imports have been erratic.

Probably the key factor in shifting import levels is that Taiwan, once the largest source of Japan's pork imports, has been absent from the trade arena since the sudden appearance of foot-and-mouth disease there in 1997 (*AO* October 2000). Imports from Korea ceased in 2000 for the same reason. However, Japan's use of the gate price system, safeguards under the Uruguay Round Agreement on Agriculture (URAA), and programs supporting pork producer revenues have strengthened domestic production at the expense of imports.

Japan's *gate price system* strongly resembles the variable levy on pork that it replaced in 1995. The gate price system is triggered when the actual price of imported pork is below the government-set standard import price. If the unit price of the imported pork (based on the price of a shipping container of meat) is less than the standard import price, the duty charged is equivalent to the differential between them plus the usual 4.3 percent ad valorem tariff. This raises the price of cheaper pork cuts in Japan. To avoid the duty, importers mix cuts of different values in containers until the container's average value is at or above the standard import price. The gate price system distorts trade because traders import cuts that they ordinarily would not buy.

In addition to the S*pecial Safeguards* of the main URAA text, Japan negotiated an additional set of safeguards for pork and beef in a side agreement. The pork safeguard is triggered when cumulative quarterly imports rise 19 percent or more over the average import volume during the same period in the previous 3 years. If Japan chooses to invoke the safeguards, it can raise the gate price to any level not exceeding an upper bound specified in its URAA commitment for the remainder of the year (or the first quarter of the following year if the trigger occurs during the fourth quarter), instead of applying the lower gate prices negotiated in the URAA.

Japan's Pork Production Stabilized in the Late 1990s, While Imports Have Been Erratic



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Japan invoked both kinds of safeguards at times in 1996 and early 1997. In response, importers stockpiled frozen pork inside and outside Japan, taking it through customs in a quarter when the safeguard did not apply. The surge of frozen stocks avoiding higher duty in place under the safeguard, however, increased the likelihood that import volumes would trigger the safeguard again in the following quarters, launching a cycle that was ended by the sudden withdrawal of Taiwan from the market.

Support for Japan's 11,700 hog farms—down from 36,000 in 1991—is through the Regional Pork Price Stabilization Fund, begun in 1995, which pays farmers the difference between the market price and a floor price that is specific to each prefecture. The market price was below floor prices ($3.50-$4.00/kg) in 2000 for about 3 million hogs sold in the first half of 2000, and the fund paid out about $85 million during the period. Check-off fees from farmers go into the fund, but most support comes from the government.

some rice and of wheat and barley for feed use have been increasingly conducted through a "simultaneous buy and sell" (SBS) process, which allows foreign exporters and domestic buyers to work together to submit bids. The Food Agency chooses bids that provide the highest margin between the import price paid to sellers and the higher (marked up) domestic resale prices charged in Japan, with the Food Agency keeping the markup.

However, the margin cannot exceed the maximum markup levels that Japan agreed to in the URAA.

The list of designated grain suppliers to the Food Agency in its traditional (non-SBS) purchases of rice, wheat, and barley within the quotas has broadened in the 1990s to include foreign-controlled firms. These changes reduce the Food Agency's role in determining what is brought into Japan, and where it comes from.

Japan's rice trade was treated as a special case in the URAA, and Japan did not convert nontariff barriers into an equivalent tariff for rice. Instead, it agreed to implement a quota which was to reach about 8 percent of domestic consumption in 2000 compared with zero in most years before 1995. However, Japan changed its policies

and decided to "tariffy" its rice trade beginning in 1999 (*AO* April 1999). It established a rice *tariff-rate quota* and an overquota tariff based on the tariff equivalent of its former nontariff barriers. The overquota tariff is so high that it effectively prohibits additional rice imports, and the change, while ending the special treatment of Japan's rice trade, did not open the door to new trade.

Japan has used the S*pecial Safeguard* mechanisms established in the URAA extensively since 1995. They allow a temporary increase in duties to one-third higher than the normal tariff if a surge in import volume or a steep decline in import prices occurs, and if the right to use safeguards had been reserved for a product in the URAA. Japan used such safeguards 28 times in the 5 years prior to April 2000, chiefly for starches, livestock products, and dried legumes.

In addition, Japan negotiated a side agreement to the URAA to establish another kind of safeguard mechanism for its pork and beef markets. At the end of 2000, Japan began proceedings to use measures under the UR Agreement on Safeguards to protect domestic dried shiitake mushroom and welsh onion production. Such safeguard measures could involve imposing a quota on imports for up to 4 years. Japan has announced that other commodities are under consideration for such protection.

Japan's *phytosanitary barriers* have blocked imports of some vegetables and fruits. After prolonged negotiations, Japan agreed in 1999-2000 to use one set of criteria for all varieties of apples, tomatoes, and nectarines from a given growing region. If phytosanitary acceptance were obtained for a growing regime for one variety in an exporting country or region of a country, it could thus be extended to other varieties from that area, saving time and expense for farmers growing products for export. Despite this advance, Japan's phytosanitary regulations on imported fruit and vegetables remain very stringent and costly to satisfy.

Agriculture in Japan

Overall, agriculture is big business in Japan. In 1998, the latest year of available data, the gross value of agricultural output was $76 billion. However, much of Japan's agriculture is carried on by relatively small farms with high labor costs. Over 2.5 million households met one of two criteria for commercial farming: selling over $4,000 of farm output in a year or farming over three-fourths of an acre. In 1998, 11.3 million people—almost 9 percent of Japan's population—resided in households engaged in commercial farming. The large number of farm households reflects the very small scale of landownership in Japan that results in a large number of people with a stake in farming.

Japan's government devotes large sums to supporting agriculture. In 1998, Japan spent over $82 billion (about 6 percent of national government expenditures) on agriculture, in such projects as improving irrigation, reshaping fields, building processing plants, and providing production subsidies. On average, Japan's consumers spend considerably more on food than U.S. consumers and the food share of living expenditures is larger—18 percent in Japan in 1994 vs. 8-10 percent in the U.S. The Organization for Economic Cooperation and Development (OECD) estimates that in 1999, consumers spent an extra $68 billion (about 1.5 percent of GDP) as a result of just some of Japan's agricultural policies.

Implications of The New Policies

Japan is the world's largest importer (by value) of pork, beef, corn, and a number of other commodities. Imports of eight commodities—pork, beef, corn, soybeans, poultry meat, coffee, wheat, and wine—each averaged near $1 billion or more per year during 1997-99. Japan is also the largest export destination for U.S. agricultural products—a $9-billion market in 2000.

The condition of Japan's domestic agricultural production is of interest to many suppliers in global commodity markets. Consumption of basic commodities in Japan is relatively stable and not likely to grow in the future because of a population growth rate near zero and the lower food needs of an aging population. In general, increases in imports of basic commodities into Japan will occur only if Japan's production decreases. The current structure of production survives in the shelter of government policies.

Japan's policies are aimed at making farms more efficient in order to preserve the existing level of agricultural production. Together with heavy support for farm consolidation, mechanization, and efficient packing, distribution, processing, and marketing, the new commodity programs encourage a smaller number of professional farmers to compete against imports in satisfying Japanese consumers. To the extent that this new set of programs succeeds, imports will not grow.

The new programs face severe hurdles. Market prices have been declining in Japan for most years in the last decade. Participating farmers will be compensated for 80 percent of a drop from previous years' average prices for many commodities. Competition from imports and from more efficient Japanese farmers not participating in the stabilization schemes will be intense. Unless farmers receive additional forms of support, so much land may exit farming that output will fall. Japan has already begun direct per-hectare payments to farmers in mountainous areas where consolidation is difficult, basing payments on multifunctionality arguments. Spending on the program in 2000, the first year, was over $300 million.

Although Japan's federal and local governments spend more in support of agriculture than the gross value of agricultural output, Japan's spending to maintain production is constrained by WTO rules. In formulating its new policies, Japan seeks to move its policies out of the "amber box" of policies that are subject to reduction because they distort trade, and to develop policies that fit in the "blue" or "green" boxes. Unlike blue box policies,

green box policies are not tied to current production or price of a commodity.

Japan's URAA commitment to cut amber-box spending involved scaling back programs that set administered prices for domestic output. These prices were usually high enough to cover most farmers' costs, and the government managed some markets to make consumers bear the costs. Now, administered prices have been eliminated, but two related questions are still not answered:

- How will the WTO classify the new policies under existing rules—i.e., amber, blue, or green box?
- How will the new policies fit within a set of international rules that might emerge in ongoing WTO negotiations over a new agreement on agricultural trade?

Japan's proposal for the WTO negotiations includes calls to allow policies to maintain domestic food production for food security and for functions other than efficient food production. Japan favors retention of the WTO blue box category and expansion of the green box category to accommodate such policies. Japan did not have policies that fit in the blue box at the time the URAA was ratified, but in its February 2001 notification to the WTO, Japan contended that its new rice programs belong in the blue box (beginning with the 1998 crop) and thus expenditures are exempt from reduction. However, many other countries are calling for elimination of the blue box category in the future. Within and outside Japan, the actual operation of the new policies, their impacts on production and trade, and their interaction with Japan's negotiating position will be watched with interest. AO

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Based in part on reports from the USDA Foreign Agricultural Service office in Tokyo, Japan.

Upcoming Reports—USDA's Economic Research Service

The following reports are issued electronically at 3 p.m. (ET) unless otherwise indicated.

April

5	*Tobacco*
10	*World Agricultural Supply & Demand (8:30 a.m.)*
11	*Cotton and Wool Outlook (4 p.m.)***
	*Oil Crops Outlook (4 p.m.)***
	*Rice Outlook (4 p.m.)***
12	*Wheat Outlook (9 a.m.)***
18	*Agricultural Outlook**
19	*Vegetables and Specialties*
24	*U.S. Agricultural Trade Update*
25	*Feed Yearbook*
	*Livestock, Dairy, and Poultry (4 p.m.)***

*Release of summary, 3 p.m.
**Available electronically only